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Real Health-Care Reform
Why America must move away from its third-party-payer system.

July 15, 2010
By Rep. Jim Marshall

The recently passed health-care-reform legislation, which I opposed, has been pilloried as "worse than 9/11" and "the end of prosperity in America forever" and "the end of America as you know it" and "the end of the republic." Utter nonsense. Its supporters have said the new law "is a triumph in terms of deficit reduction" that will "significantly reduce long-term health-care costs" and "not add one dime to the deficit" and "strengthen Medicare" and "reduce premiums and out-of-pocket costs." Unfortunately, this is also nonsense. Structurally, the legislation is just more of the same -- a few box cars added to a runaway economic freight train hauling the nation toward bankruptcy.

The federal government's current regulation of health care, encapsulated in fine print on merely 132,000 pages, is costly, clumsy, inefficient, and inequitable. Doing more of the same to achieve cost containment will be painful and disruptive to medical providers and the public, making serious cost containment highly unlikely. So a fair observer would conclude that the 2010 reform legislation will help millions of Americans in different ways, hurt millions of Americans in different ways, and generally lead to increased costs. Details to follow.

It didn't have to be this way. American employers inadvertently created the conditions for health care's eventual hyperinflation by offering comprehensive health-insurance and retirement plans to evade wage and price controls imposed during World War II. Later, government officials followed their lead by essentially adopting a health-insurance model for Medicare and Medicaid. Third-party payers (insurance companies, self insurers, and government) now make some 88 percent of American health-care payments. (The new law will increase this percentage.) As a result, most patients and providers see little or no marginal cost associated with millions of health-care decisions made daily. Yet one way or another -- through taxes, premiums, lower wages, lower profits, and stunning increases to our national debt -- we are all paying the tab. And that tab is at least twice what it should be. Some 17 percent of U.S. GDP is devoted to health care, roughly double the average for the rest of the developed world, and yet impartial experts rate our health-care system as average -- the best in some respects, but pretty poor in others.

Over the decades since its introduction, our comprehensive third-party-payer system gradually increased health care's annual inflation rate and introduced Soviet-style inefficiencies that produce mountains of waste, fraud, and abuse. (By some counts, approximately $60 billion is stolen each year from Medicare and Medicaid alone.) The change has been insidious. Americans know health care is much too expensive; they just don't know why. That's because, for most Americans, health care is now synonymous with health insurance. As repeatedly evidenced in the reform debate, the two are so conflated that it is difficult even to imagine the separate influence of comprehensive insurance on health-care costs, much less honestly discuss it.

Economists widely agree that health care's third-party-payer system increases costs by introducing the "wrong incentives." But they cannot quantify how much. Though computer modeling could narrow the range of possibilities, too many variables and assumptions are required to precisely estimate how health-care costs would have evolved without comprehensive health insurance.

To get some feel for the degree of its likely impact, however, just think about what happens to the total cost of dinner when friends agree to split the tab. Those familiar with this choice know that the total cost usually increases, sometimes substantially. Now imagine what happens if complete strangers agree to split the tab. Most conclude that the total cost is likely to be even higher, since strangers face less social pressure for restraint. Now suppose the strangers can individually choose any restaurant, but they will still split the tab. Total costs go up yet again. Now extend this analogy to our entire population. Suppose all Americans split the tab for dinner every evening. They needn't go to dinner, but they will still be splitting the tab every night. Think about what happens to our economy and individual wealth over time.

Someone familiar with game theory would describe this as a classic prisoner's dilemma. The welfare of all is furthered by each consuming modestly to keep down the tab. But for each individual, there is essentially no marginal cost for consuming a lavishly expensive meal. Americans with a social conscience initially consume modestly. But many others order the most expensive food and drink. The tab is consequently much higher than the modest consumers anticipated. Obviously, their fellow Americans are not holding back. So gradually they lose restraint as well.

Unable to escape or manage its prisoner's dilemma, America's nightly tab steadily grows. Many Americans cut back to one meal a day, stuffing themselves in the evening. Bankruptcy courts are flooded. Welfare programs expand to permit the poor to eat. Low-end fast-food chains disappear. High-end restaurants dominate the national economy. As the tab steadily grows, families have less money for rent, for clothing, for education, for health care. America's global economic competitiveness falters. Her citizens are poorer and sicker. Entreaties to consume responsibly have little effect. Eventually, Congress limits the consumption menu. Lawsuits and protests against socialism follow.

Health care's third-party-payer system suffers from similarly perverse incentives. And it has a similar impact upon our national economy and individual wealth. Few Americans realize we are devoting at least twice what we should to health care because we are splitting the tab through taxes, insurance premiums, lower wages, lower profits, and stunning increases in government debt. Over decades, health care's distorted third-party-payer incentives have caused providers to do more and more tests, procedures, and consultations. This "more and more" has become the accepted standard of care. That might be fine if we could afford it, but we obviously cannot. Forty-seven cents of each health-care dollar comes from taxpayers, the lion's share from federal taxpayers. Medicare's trustees estimate its current unfunded liabilities to be nearly $40 trillion. And that represents only part of our health-care tab.

Our third-party-payer health-care system bankrupts individuals, and it is bankrupting the nation. Even worse, there are many thoughtful commentators -- such as David Goldhill (author of the 2009 Atlantic article "How American Health Care Killed My Father") or Shannon Brownlee (author of the 2007 book Overtreated) -- who believe health care's third-party-payer system not only makes us poorer but also makes us sicker. Too much health care can be costly and dangerous.

Because it adds less revenue than cost and increases our reliance upon third-party payers, the reform legislation stealthily hurries us along toward bankruptcy. Meanwhile, we naïvely seek to cure our health-care cost woes by lining up the usual suspects: greedy or dishonest trial lawyers, health insurers, drug companies, and medical providers. Reforms focused on each of these can lower costs, but not by much.

The Congressional Budget Office (CBO) estimates that premiums for medical-malpractice insurance, lawsuit settlements and related costs, and waste due to the practice of defensive medicine increase overall health-care costs by about 2.5 percent. Part of this expense is not unique to health care; it's a routine cost for providing services or products. The CBO attributes only one-fifth of the cost increase to the practice of defensive medicine. That's because, for the most part, providers do not change their practice patterns in response to comprehensive medical-malpractice reform. They keep following the accepted standard of care. No surprise there. A medical provider's duty is to patient care, not to national solvency. Providers will lead the way to less care if doing less is proven to be in the patient's interest. Our third-party-payer system essentially assures that, for the many tests, procedures, and consultations that fall in the wide range between demonstrably "not enough" and demonstrably "too much," the accepted standard of care will hover just below demonstrably "too much." Ironically, this conclusion is bolstered by widespread anecdotal testimony from medical providers that they practice defensive medicine. They all know Americans are overtreated; too few know why.

Insurance and drug-company profits combined increase costs by 2 or 3 percent. Of course, dramatically cutting the role of third-party payers would substantially reduce the costs associated with making and paying health-insurance claims. More than 1 million employees for providers and payers handle these claims. We carry the cost as part of our overall health-care tab.

Finally, some providers do milk the current system. No one knows how many or how much. Atul Gawande's award-winning 2009 New Yorker article, "The Cost Conundrum," illustrates how difficult it is to find the answer. While all professions have problems with milking, health care's third-party-payer system makes milking easier and somewhat victimless. In fact both patient and provider often view the third-party payer as the enemy, so much so that some providers see themselves as modern day Robin Hoods, working and breaking the rules of the system to meet the needs of their patients.

Blaming our runaway health-care costs on insurers, drug manufacturers, lawyers, and medical providers distracts us from focusing on the principle culprit: our excessive dependence on a third-party-payer system. That's what truly drives our cost dilemma. And that's what Americans must focus on if we have any hope of overcoming the entrenched habits and interests that maintain this utterly wasteful and costly status quo.

We should slowly migrate away from the current system. Absent some acceptable alternative, third-party payers could continue offering comprehensive service to those who cannot effectively manage health care on their own. Most Americans, however, should participate in a sufficiently robust private market for health-care services, a market that settles on a price and also sets the expected standard of care. Today, there is no such market for health care, nor is there one for most military goods and services. The Pentagon tackles this price-for-quality problem with thousands of "acquisition specialists" only because it has few market options. And its specialists have paid $640 for a $12 toilet seat and $436 for a $7 to $10 claw hammer. Health care has a market option.

Employers led us into this mess; they may be able to lead us out, particularly if government acts as a facilitator and not an obstacle. Both private and public employers should move from offering comprehensive plans to offering high-deductible or catastrophic ones plus medical savings accounts the employee can tap for any purpose once the amount on deposit exceeds a specified level. These accounts should be portable and roll from year to year. Organized labor should join this effort. Although unions would have a lesser role in health-care negotiations, their members would most likely see higher wages over time as employers realized lower health-care costs.

Medicare and Medicaid would likely remain unchanged for the near future, but would realize savings as costs dropped. In time, however, Medicare might introduce individual Medicare Accounts owned and managed by participants, inheritable upon death and backed by catastrophic insurance. Medicaid might do something similar. Each would limit these programs to those who could competently manage their own medical affairs either directly or through a representative.

With most patients managing their own money, more providers would probably choose primary care over sub-specialties. More responsibility for managing health-care costs would encourage Americans to better manage their own health. Overtreatment would drop dramatically, as would costs. Quality would likely improve as well. Public health surely would. Lower costs would improve access for those with modest means. To accelerate this process, government might consider legislation requiring price transparency in health care plus best prices for cash. Otherwise, weaning Americans from third-party payers will go very slowly. Shopping for price is impractical, if not impossible, in our current system.

Our third-party-payer dilemma was decades in the making. We mustn't take that long to correct it. Without real health-care reform, we will continue to waste 10 percent or more of our national wealth and never find an appropriate balance between health care and other priorities. Unless we significantly reduce the role of third-party payers in health care, we will surely bury future generations of Americans in debt.

Not convinced? See if you can find some strangers willing to split the tab for dinner. Americans usually aren’t so foolish.

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